Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Runner	Analyst:	Roger Lackey	Bill Number:	AB 1924
Related Bills:	None	Telephone:	845-3627	Introduced Date:	02-15-2000
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Enterprise Zones/Aerospace Training Competitiveness Improvement Program/Credit

SUMMARY

Under the Government Code, this bill would require the Trade and Commerce Agency (TCA) to design, develop, and oversee the operation of a 36-month Aerospace Training Competitiveness Improvement Program within one or more designated enterprise zones.

Under the Bank and Corporation Tax Law (B&CTL), this bill would provide a credit to a taxpayer equal to the amount paid or incurred during the income year for the overhead costs training employees under terms of an Aerospace Training Competitiveness Improvement Program. The program must be provided for a taxpayer’s specific business unit located within a designated enterprise zone.

This analysis will address the Government Code provision only as it impacts the programs and operations of the Franchise Tax Board.

EFFECTIVE DATE

This bill specifies that the tax credit would be effective for income years beginning on or after January 1, 2001, and before January 1, 2004. The Aerospace Training Competitiveness Improvement Program and the related credit would be repealed on January 1, 2004, and December 1, 2004, respectively.

SPECIFIC FINDINGS

Under the Government Code, existing state law provides for the designation of enterprise zones. Using specified criteria, the TCA designates these economic development areas from the applications received from local governing bodies. TCA has designated the maximum 39 enterprise zones authorized under existing law.

Under the Revenue and Taxation Code, existing state law provides special tax incentives for taxpayers conducting business activities within enterprise zones. These incentives include a sales or use tax credit, hiring credit, business expense deduction, and special net operating loss treatment. Two additional incentives include a net interest deduction for businesses that make loans to businesses within an enterprise zone and a tax credit for employees working in an enterprise zone.

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Also, **state law** allows a taxpayer to deduct ordinary and necessary business expenses from the taxpayer's income when calculating the taxpayer's tax liability. Such expenses would include those expenses related to overhead costs.

Under the Government Code, **this bill** would require the TCA to design, develop, and oversee the operation of a 36-month Aerospace Training Competitiveness Improvement Program within one or more designated enterprise zones.

This program would function as a pilot project to evaluate the impact of training on competitiveness for aerospace contractors and suppliers doing business in this state. The purpose of this program would be to determine the feasibility, affordability, and effectiveness of reduced training cost in creating additional jobs in the aerospace and defense industry segment. In addition, the TCA would develop criteria to evaluate the project's performance and effectiveness during its lifetime.

This bill would provide both of the following:

- Reimbursements to community colleges operating an aerospace training center inside a designated enterprise zone for costs of providing common employee training services to two or more aerospace contractors or suppliers or both.

- A credit against state taxes of aerospace contractors or suppliers for overhead costs incurred while providing employee training during normal working hours.

T**his bill** would limit the credit a taxpayer may claim to the actual amount paid or incurred during the income year for overhead costs of the taxpayer's specific business unit located within the designated enterprise zone in which an Aerospace Training Competitiveness Improvement Program exists for training employees. This bill would require the taxpayer to certify that the tax credits claimed would be applied dollar-for-dollar against the overhead costs of the specific business unit, located within a designated enterprise zone, which provided the training that qualified for the credit.

Any excess credit would be allowed to be carried over indefinitely.

Since **this bill** does not specify otherwise, the general rules in state law regarding credits, including division of the credit among taxpayers who share the costs, would apply.

Policy Considerations

This bill would permit a credit for taxpayers under the B&CTL, but does not permit the same credit for taxpayers under the Personal Income Tax Law (PITL).

This bill would provide a 100% credit equal to the overhead costs of the specific business unit for training employees. Generally, credits are equal to a percentage of the expenses or costs associated with the credit.

Other EDA credits explicitly require employees who are the subject of the tax incentives to be employed in the EDA. While this bill would require the training center to be located in the EDA, the training would be available to any of the taxpayer's employees, regardless of whether the employee worked in the zone.

Other EDA credits limit the amount of the credit by allowing the credit to be used only against the amount of tax that is imposed on the taxpayer's business income attributable to that EDA. This credit would be allowed against the taxpayer's full tax liability, regardless of where the net income subject to tax was earned.

There may be conflicting tax policies when a credit is provided for an expense item for which preferential treatment is already allowed in the form of a deduction. This proposed credit would have the effect of providing a double benefit for taxpayers that deduct the expense of overhead with their ordinary and necessary business expenses. However, eliminating the double benefit by expressly denying the deduction if the credit is claimed or making an adjustment to reduce basis would create a state and federal difference, which is contrary to the state's general conformity policy.

Implementation Considerations

This bill does not define the term "overhead costs." The lack of a clear definition could lead to disputes between taxpayers and the department regarding the correct interpretation of the term and, therefore, the amount of the resulting credit. Since over can be defined as all administrative or executive costs incident to the conduct of a business, it would be helpful if the bill detailed those costs eligible for the credit.

This credit is limited to overhead costs of specific business units located in a designated EDA, but does not specify a criterion to determine when a specific business unit is considered to be located "in" an EDA for purposes of the credit.

This bill would provide a credit for aerospace contractors or suppliers or both for costs incurred while providing employee training within the aerospace and defense industry. Since this bill would include the suppliers of the aerospace industry, this credit could apply to businesses outside the aerospace industry. For example, an office supply company may provide writing utensils, paper, etc. to a business that provides for the training in the aerospace industry. Under the provisions of this bill, the office supply company could be considered to be a supplier of the aerospace industry and as a result could be eligible for the credit provided for by this bill.

Recent credits have been enacted with a carryover limit since experience shows credits are typically used within eight years of being earned. Without a carryover limit, the department would be required to retain the carryover credit on the tax forms indefinitely.

The credit is repealed on December 1, 2004, to allow fiscal year filers to claim the credit for all the calendar months of their 2003 year. However, the Aerospace Training Program under the Government Code is repealed on January 1, 2004. This inconsistency in dates may cause confusion over whether the credit is allowed to fiscal year filers based on costs paid or incurred during 2004 following repeal of the related provisions of the Government Code added by this bill.

FISCAL IMPACT

Departmental Costs

Once the implementation concerns are resolved, this bill would not significantly impact departmental costs.

Tax Revenue Estimate

It is not possible to predict in advance the number and location of enterprise zones that would be selected for the pilot program, “qualified” overhead costs related to aerospace training, or the response of potential contractors/suppliers in such zones to the credit incentive.

Based on departmental data for tax year 1996, the total revenue loss for the existing 38 enterprise zones was $39 million (approximately $1 million on average per zone).

BOARD POSITION

Pending.